Nos. 78-1585 and 78-1681

# In the Supreme Court of the United States

OCTOBER TERM, 1978

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STATE OF LOUISIANA, PETITIONER

*v.*

FEDERAL ENERGY REGULATORY COMMISSION

---

STATE OF TEXAS, PETITIONER

*v.*

FEDERAL ENERGY REGULATORY COMMISSION

---

*ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT*

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## BRIEF FOR THE FEDERAL ENERGY REGULATORY COMMISSION IN OPPOSITION

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## OPINIONS BELOW

The opinion of the court of appeals (Pet. App. B)[1] is reported at 587 F.2d 716. The opinions and orders of the Federal Power Commission[2] (Pet. Apps. C and D) are not reported.

## JURISDICTION

The judgment of the court of appeals was entered on January 11, 1979 and its order denying a petition for rehearing (Pet. App. A) was issued on February 8, 1979. The petition for a writ of certiorari in No. 78-1585 was filed on April 16, 1979 and in No. 78-1687 on May 7, 1979. This Court's jurisdiction is invoked under 28 U.S.C. 1254(1).

## QUESTIONS PRESENTED

1. Whether a state may divert to another purchaser gas it owns that was previously dedicated to

[1] Unless otherwise indicated, all citations herein to the actions of the court of appeals and the Commission will be to the appendices in the State of Louisiana's petition, cited as "Pet. App." "R." refers to the certified record before the court of appeals.

[2] Pursuant to the provisions of the Department of Energy Organization Act, Pub. L. No. 95-91, 91 Stat. 565 (to be codified as 42 U.S.C. 7101 *et seq.*), the Federal Power Commission ceased to exist on September 30, 1977 and most of its functions and regulatory responsibilities, including those relevant to this case, were assumed by the Federal Energy Regulatory Commission effective October 1, 1977. Hereinafter, the term "Commission" refers to the FERC or the FPC depending on whether the events referred to occurred before or after October 1, 1977.



an interstate pipeline by the state's lessee, without prior authorization from the Commission under Section 7 of the Natural Gas Act to abandon service to the pipeline.

2. Whether a requirement that states obtain abandonment authority under Section 7 of the Natural Gas Act unconstitutionally intrudes upon state sovereignty.

## STATUTE INVOLVED

Section 7(b) of the Natural Gas Act, 15 U.S.C. 717f(b), provides:

> No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Commission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience and necessity permit such abandonment.

## STATEMENT

On June 1, 1965, the State of Texas, through its School Land Board, leased to Superior Oil Company ("Superior") certain state owned acreage offshore

from Texas (Texas Pet. 3).[3] On May 7, 1971, Superior contracted with Natural Gas Pipeline Company of America ("Natural") to sell to Natural for resale the natural gas produced from the leased area (Pet. App. 5a, 16a).

Superior obtained from the Federal Power Commission a certificate of public convenience and necessity authorizing the sale under Section 7 of the Natural Gas Act, 15 U.S.C. 717f, and service commenced (Pet. App. 4a-5a).[4]

Under the original leases Texas did not take its royalty payments in kind (Pet. App. 4a n.5); instead, Superior sold all of the gas produced and Texas received its royalties in the form of a share in the proceeds from the sale. However, in January 1974, Texas, Superior and Natural entered into a new agreement which, *inter alia,* authorized Texas at its option to require payment of all royalties in kind (Pet. App. 5a; R. 17).[5] The Commission granted Superior's request for an amendment in its certificate

[3] Petitioner Louisiana intervened in the Commission proceedings (Pet. App. 21a) and petitioned the court of appeals for review of the Commission's order (Pet. App. 3a). Louisiana, however, has no interest in any of the gas involved in this case.

[4] The Commission's certificate was of unlimited duration, as was the term of the lease between Texas and Superior (Pet. App. 30a).

[5] Texas also retained the right from time to time to deliver the gas under the Superior-Natural sale/purchase agreement (R. 18). The provision of the agreement dealing with royalty shares also established that the rights and obligations of Superior and Natural were subject to receipt of all necessary Commission approvals (*ibid.*).



to reflect the January 1974 agreement, but noted that it was not approving all of the terms of the agreement. It specifically observed that it was not granting the abandonment authority which Superior was required to obtain under Section 7(b) of the Act before certificated service could be terminated (Pet. App. 20a).

On April 25, 1975, Texas notified the Commission that effective May 1, 1975, it was electing to take its option royalty in kind (Pet. App. 5a, 20a). Effective the same day Texas contracted with Public Service Company of North Carolina, Inc. ("Public Service") for that company to buy for a limited period Texas' royalty gas (Pet. App. 5a, 20a; R. 10-14).

However, Transcontinental Gas Pipeline Co. ("Transco"), the only company with the capacity to transport the gas (R. 2), would not agree to do so until the Commission ruled that it did not have to approve abandonment of Superior's service to Natural (Pet. App. 20a). Public Service accordingly petitioned the Commission for a declaratory order that the Commission had no authority under the Natural Gas Act to require abandonment authorization before the royalty gas could be transported by Transco (*id.* at 5a, 19a).

The Commission held that neither Texas nor its leasing agency was a natural gas company within the terms of the Natural Gas Act (Pet. App. 25a). However, since Texas had chosen to do business through a regulated natural gas company and that company had dedicated the gas, Texas was bound by the obligation to serve Natural adhering under fed-

eral law to the gas pursuant to the previously issued certificates (*id.* at 29a). The Commission therefore required Superior and Texas to obtain abandonment authority before Texas would be permitted to divert the gas to Public Service (*id.* at 32a).

The court of appeals affirmed (Pet. App. 3a-13a). Accepting the Commission's determination that Texas was not a natural gas company for purposes of the Natural Gas Act, the court, relying on *California* v. *Southland Royalty Co.*, 436 U.S. 519 (1978), held that the combination of circumstances present in this case had given rise to a continuing service obligation which required Commission authorization before certificated service could be abandoned (Pet. App. 10a). The court concluded that the service obligation had attached to the gas when it was certificated and service began, and that it was immaterial that Texas was not a natural gas company because it is the dedication of the gas, not the identity of the party, that creates the service obligation (*id.* at 7a-10a). The court further held that this result is not an unconstitutional intrusion on state sovereignty under *National League of Cities* v. *Usery*, 426 U.S. 833 (1976), because the state's business operation is "indistinguishable from like commercial activities of private business" (Pet. App. 12a).

## ARGUMENT

The decisions of the Commission and the court of appeals in this case reflect a narrow application of the principle underlying *California* v. *Southland*, 436



U.S. 519 (1978), that once natural gas has been dedicated to interstate service, " 'there can be no withdrawal of that supply from continued interstate movement without Commission approval.' " *United Gas Pipeline Co.* v. *McCombs*, Nos. 78-17 and 78-249 (June 18, 1979), slip op. 13. The court of appeals correctly held that ownership by a State of some of the previously dedicated gas creates no exception to this "fundamental component of the regulatory scheme." *McCombs, supra*, slip op. 8. There is no reason for the Court to re-examine the question under the terms of the Natural Gas Act. And since all that is involved is regulation of business activity by a State in the interstate gas market, no impermissible intrusion into inherently governmental activities of the States results.

1. In *California* v. *Southland Royalty Co., supra*, the Court held that once natural gas has been dedicated to an interstate service within the Commission's jurisdiction, that service must continue until abandonment of that service is authorized under Section 7(b) of the Natural Gas Act, 15 U.S.C. 717f(b), without regard to any intervening changes in the relationships between the lessee and the lessor of the producing properties.[6]

[6] In *Southland*, the lessor of gas-producing acreage dedicated the production to interstate commerce. When the lease expired, the lessor-reversioner sought to sell the remaining reserves in intrastate commerce. The Court held that the gas was subject to "a federal obligation to serve the interstate market until abandonment authorization had been obtained."

Under *Southland* it is the regulatory status of the gas, not the legal status of those with interests in its production, that renders Section 7 controlling. Intervening "[p]rivate contractual arrangements might shift control of the [gas] and thereby determine *who* is obligated to provide that service, but the parties may not simply agree to terminate the service obligation without the Commission's permission." 436 U.S. at 527. The court of appeals thus correctly held "that an entity's status as a 'natural gas company' is largely irrelevant to the question of whether that entity must seek abandonment authorization under § 7(b)" (Pet. App. 7a).

The court of appeals also correctly rejected petitioners' claim that *Southland* is distinguishable because a state can never be a natural gas company. As the court of appeals explained (Pet. App. 9a):

> Petitioners seek to distinguish the instant case from *Southland* on the grounds that the owners of the reversionary interest in *Southland* could become "natural gas companies," while Texas can never achieve this status. This may well be true. The argument, however, overlooks the major point of *Southland*—that it is the *dedication* of the gas that creates the service obligation. Indeed, in *Southland*, the Court refused to reach the question of whether the owners were "natural gas companies." Instead, the Court pointed out that whether or not the owners were "natural gas companies" was "[largely] beside the point, for the obligation to serve the interstate market had already attached to the *gas*, and respondents became obligated to continue that servive when they assumed control of the gas." *Id.* at 528, 98 S.Ct. at 1960.

436 U.S. at 526. This obligation prevailed over the parties' private contractual arrangements and state property law defining interests in gas and gas-producing acreage.



This conclusion finds strong support in recent legislation.

First, in the Alaska Natural Gas Transportation Act of 1976, Pub. L. No. 94-586, 90 Stat. 2903, 15 U.S.C. 719 *et seq.*, Congress included a provision specifically authorizing the State of Alaska to withdraw royalty gas from "the interstate market" (Section 13(b), 15 U.S.C. 719k(b)),[7] but only on certain conditions. Thus, Section 13(b) of that Act specifies that such withdrawal is permitted only "to the extent its contracts for the sale of royalty gas so provide," and directs the Commission to "issue all authorizations necessary to effectuate such * * * withdrawal." These provisions would have been unnecessary if states already had authority under the Natural Gas Act to withdraw royalty gas without Commission approval under Section 7(b) merely because

[7] Section 13(b) provides:

> The State of Alaska is authorized to ship its royalty gas on the approved transportation system for use within Alaska and, to the extent its contracts for the sale of royalty gas so provide, to withdraw such gas from the interstate market for use within Alaska; the Federal Power Commission shall issue all authorizations necesary to effectuate such shipment and withdrawal subject to review by the Commission only of the justness and reasonableness of the rate charged for such transportation.

they were not "natural gas companies." The implication is that Congress believed states other than Alaska have no such authority.

Second, in the Natural Gas Policy Act of 1978, Pub. L. No. 95-621, 92 Stat. 3350 ("NGPA"), Congress reviewed this Court's decision in *Southland* and specifically provided for certain limitations on its future extension that are not pertinent here,[8] but it did not disturb *Southland's* basic holding as applied to gas that, as here, was dedicated to interstate commerce prior to the date of the decision. Moreover, the NGPA contains a special pricing provision for the royalty or other interests of states in natural gas, but that provision expressly does not apply to "natural gas which was * * * committed or dedicated to interstate commerce [under the Natural Gas Act] on the day before the date of the enactment of this Act * * *." Section 106(b)(2)(A) of the NGPA, 92 Stat. 3365. This further confirms that a state's royalty interest in dedicated gas is subject to established concepts of dedication under the Natural Gas Act.

[8] See Section 2(18) of the NGPA, 92 Stat. 3354. Section 2(18)(A)(ii) defines for purposes of the 1978 Act, gas that is "committed or dedicated to interstate commerce" as gas "which, if sold, would be required to be sold in interstate commerce (within the meaning of the Natural Gas Act) under the terms of any contract, any certificate under the Natural Gas Act, or any provision of such Act." Section 2(18)(B)(iii) excludes from this definition gas that was not being sold in interstate commerce on May 31, 1978, if on that date neither the person who caused the gas to be dedicated or such person's successor in interest (other than a reversionary lessor) "had any right to explore for, develop, produce, or sell such natural gas." Since the gas involved here was being sold in interstate commerce on May 31, 1978, the exclusion is inapplicable.



The ruling of the court of appeals is, in any event, a proper application of the basic purpose of the Natural Gas Act as identified in *Southland* and other cases. The requirement that abandonment be authorized by the Commission under Section 7 is intended "to protect those communities presently depending on the flow of gas pursuant to a certificate of unlimited duration already issued." *Southland Royalty Co., supra*, 436 U.S. at 530; *Sunray Mid-Continent Oil Co.* v. *FPC*, 364 U.S. 137, 142, 156 (1960). The protection afforded to such communities would be significantly vitiated if, pursuant to the terms of agreements between private producers and states, dedicated natural gas could be withdrawn from an interstate market at will.

For the reasons identified in *Southland*, there is no inequity or inconsistency with the regulatory scheme in holding lessor-states, like lessors who are private parties, to the service obligations of the Natural Gas Act. By authorizing Superior to sell its gas under an interstate certificate to Natural, Texas itself authorized changes in the regulatory status of the gas that could be annulled only by the means Congress has specified. See *United Gas Pipeline Co.* v. *McCombs, supra*. The Court's description of the private lessors in *Southland* applies equally to Texas and its agencies in this case, which are " 'mineral lease owners who entered into a lease that permitted the lease holders to make interstate sales.' * * * They did not object when [Superior] sought a certificate

from the Commission. * * * Having authorized [Superior] to make interstate sales of gas, [petitioners] could not have expected those sales to be free from the rules and restrictions that from time to time would cover the interstate market." *Southland Royalty Co.*, *supra*, 436 U.S. at 528-529.

2. Contrary to the claim of petitioner Texas (Texas Pet. 15-16), application of the regulatory requirements in Section 7 of the Natural Gas Act to gas in which a State has an interest does not unconstitutionally intrude upon State sovereignty by displacing "the States' freedom to structure integral operations in areas of traditional governmental functions * * *." *National League of Cities* v. *Usery*, 426 U.S. 833, 852 (1976). To the extent that a State enters the arena of commerce by selling its natural resources in the interstate marketplace, it is subject to Congress' paramount power to regulate interstate commerce. "It should be evident * * * that the running of a business enterprise is not an integral operation in the area of traditional government functions." *City of Lafayette* v. *Louisiana Power & Light Co.*, 435 U.S. 389, 424 (1978) (Burger, C.J., concurring). Accord, *National League of Cities*, *supra*, 426 U.S. at 854, n.18; *United States* v. *California*, 297 U.S. 175 (1936); *Parden* v. *Terminal Ry.*, 377 U.S. 184 (1964); *California* v. *Taylor*, 353 U.S. 553 (1957). Even if regulation under the Natural Gas Act has an incidental effect on Texas' ability to generate revenues devoted to schools or other uses,[9] the court of appeals correctly held that such an effect "comes nowhere near constituting a federal usurpation of state control over public education in Texas" (Pet. App. 12a). See also *National League of Cities*, *supra*, 426 U.S. at 856 (Blackmun, J., concurring).



## CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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JUNE 1979

[9] This Court has long rejected the suggestion that federal regulation is impermissible if it impinges on a state's revenue raising opportunities. See, *e.g.*, *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 608, 612-614 (1944). Cf. *In re Permian Basin Area Rate Cases*, 390 U.S. 747, 822 n.114 (1968); *Oklahoma ex rel. Phillips* v. *Guy F. Atkinson Co.*, 313 U.S. 508, 534 (1941).

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